

## **AUTHORITY OF USDA UNDER 1921 PACKERS AND STOCKYARDS ACT**

By  
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975 Bascom Mall  
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June 5, 2000

**SUMMARY**

- A. The Secretary of Agriculture has responsibility for the efficient regulation of markets under the Packers and Stockyards Act.
- B. Agencies are not bound by their own prior interpretations; indeed, they are expected to change interpretations over time.
- C. Great deference is to be given agencies in the interpretation of the statutes they are authorized to administer.
- D. Deference is to be given even when an agency's interpretation represents a sharp break from the past.
- E. Federal courts sometimes "predict" how a state court would interpret a state law when such an interpretation has yet to be made by the state court. These "predictions" of state court action do not limit the state courts.
- F. Therefore, in the absence of a definitive U.S. Supreme Court interpretation, an agency is not caused by prior precedent of its own or by judicial interpretation of statutes not yet interpreted by the agency.

**Conclusion:** The USDA has the authority to issue the proposed guidelines.

## AUTHORITY OF USDA UNDER 1921 PACKERS AND STOCKYARDS ACT

I have been asked to prepare an analysis of:

1. whether the USDA has legal authority to promulgate specific proposed guidelines (attached) defining undue price preference and discrimination under the 1921 Packers and Stockyards Act; and
2. whether such guidelines must conform to rulings by Administrative Law Judges and federal courts interpreting the act in absence of such regulations.

My conclusion, upon review of the pertinent material, is that USDA does have the authority to issue such guidelines and that the provisions of such guidelines need not follow past interpretations by any body other than the United States Supreme Court authority.<sup>1</sup>

Under the Packers and Stockyards Act, responsibility for the efficient regulation of market agencies and packers lies with the Secretary of Agriculture (USDA) and its Judicial Officer (JO) acting in his stead.

*Capitol Packing Co. v. U.S.*, 350 F.2d 67, 37 (10th Cir. 1965). It has been held that the Packers and

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<sup>1</sup> Administrative rules may be legislative or interpretive. There are four main differences between legislative rules and interpretative rules. First, a legislative rule is as binding (on the public, the agency and courts) as a statute, where an interpretative rule is not binding. Second, agencies must use notice and comment procedures under APA 8553 in adopting legislative rules, which is not the case for interpretative rules. Third, an agency has the power to issue binding legislative rules only if, and to the extent Congress has authorized it to do so. By contrast, any agency can issue interpretative rules. Fourth, legislative rules have more leeway to deviate from the specific obligations imposed on the issuing agency by congress (as long as the rule is within the scope of rulemaking authority conferred on the agency by statute). Kenneth Culp Davis, *Administrative Law Treatise*, Vol. 1, § 6, f., 234 (19).

Stockyards Act applies to the poultry industry and gives the Secretary of Agriculture considerable authority and duties in respect to regulation of the industry. *Jackson v. Swift Eckrich, Inc.* 836 F.Supp 1447 (W.D.Ark.1993), affirmed 53 F.3d 1452, 1455. This chapter's coverage was to encompass the complete chain of commerce and give the Secretary of Agriculture complete regulatory power over packers and all activities connected therewith. *Bruhn's Freezer Meats of Chicago, Inc. v. U. S. Dept. of Agriculture*, 438 F.2d 1332, 1339(8th Cir. 1971). Moreover, according to *U.S. v. O'Rourke*, 116 F.Supp. 857 (N.D. Ill. 1953), the purpose of this chapter is to insure, without discrimination, reasonable stockyards and services, reasonable and non-discriminatory rates, and the elimination of unjust or discriminatory practices. In light of the construction and purpose of the Packers and Stockyards Act, along with general notions of administrative law, the USDA is authorized to promulgate regulations interpreting a provision ("undue preference and price discrimination") even without explicit Congressional authority to promulgate such specific regulations. As long as the guidelines are within the scope of delegated power, are reasonable, and not arbitrary and capricious, an agency can "fill in" what it deems appropriate.

In *American Hospital Association v. NLRB*, 499-U.S. 606, 613 (1991), the United States Supreme Court held that if Congress had intended to "curtail in a particular area the broad rulemaking authority granted in § 6, we would have expected it to do so in language expressly describing an exception from that section or at least referring specifically to the section." 499 U.S. at 125. The court went on to say that, given the extensive notice and comment procedures followed by the Board and its thorough analysis, it (the court) would not have been troubled even if there were inconsistencies between the current rule and prior NLRB pronouncements. 499 U.S. at 127. It is to be expected that agencies will change policies with time, and just because an agency changes it's mind does not undermine the validity

of a rule that is based on substantial evidence and supported by a "reasoned analysis". *Motor Vehicles Mfrs. Assn. of U.S. v. State Farm Mutual Auto. Ins. Co.*, 463 U.S. 29, 42, 57 (1983). Moreover, neither antiquity nor contemporaneity with a statute is a condition of validity. *Smiley v. Citibank*, 517 U.S. 735, 740 (1996). Deference is accorded to agencies because of a presumption that Congress, when it left ambiguity in a statute meant for implementation by an agency, understood that the ambiguity would be resolved, first and foremost, by the agency, and desired the agency (rather than the courts) to possess whatever degree of discretion the ambiguity allows. Respect may be accorded to a pertinent federal court decision but slavish deference is not required. However, the agency would not have the same wide discretion if the United States Supreme Court has spoken specifically on the interpretation at issue.

Deference is denied only when positions are wholly unsupported by regulations, rulings, or administrative practice. *Bowen v. Georgetown Univ. Hospital*, 488 U.S. 204, 212 (1988). Once the ordinary rule of deference is accorded, the question is not whether an interpretation at issue represents the best interpretation of the statute but only whether it represents a reasonable interpretation. As noted earlier, a legislative rule can impose distinct obligations on members of the public in addition to those imposed by statute, as long as the rule is within the scope of rulemaking authority conferred on the agency by statute.

When an agency makes a rule, the rule can be freely overturned by the agency itself and an overruling may usually be retroactive. Therefore, rules based on an agency's precedents are not usually binding on the agency, for the agency, like a court, may overrule its precedents and apply a "new" rule retroactively to the facts of the overruling case. For example, a district court held that the National Labor Relation Board's "Statement of Purpose" that was published in the Code of Federal Regulations was binding on a Regional Director in a pre-hearing investigation, but a court of appeals reversed on

the ground that "the statement of procedure is simply a guideline for Board Personnel; it does not constitute formal rules or regulations that could appropriately serve as a standard binding the board to a particular form of pre-hearing investigation in every case." *Modern Plastics Corp. v. McCulloch*, 400 F.2d 14, 19 (6th Cir. 1968).

In *Bosma v. USDA*, 754 F.2d 804, 807 (9th Cir. 1984), Bosma challenged the Judicial Officer's reversal of the ALJ's finding. The court held that on appeal from or review of the initial decision (by the ALJ), the agency has all the powers which it would have in making the initial decision except as it may limit the issues on notice or rule. *Federal Communications Commission v. Allentown Broadcasting Corp.*, 349 U.S. 358, 364 (1955). A reviewing court may consider the Administrative Law Judge's findings as part of the record in determining whether substantial evidence supports the Judicial Officer's decision.

In *Southwest Sunsites Inc. v. FTC*, 785 F.2d 1431, 1435 (9th Cir. 1986), an ALJ dismissed a complaint based on the agency's failure to adhere to a previous standard. The Commission applied a "new" standard to define deception (The FTC's organic Act empowers it to proceed against "unfair or deceptive acts or practices in or affecting commerce") and the petitioners claimed that the application of the new standard defining "deception" violated the Administrative Procedure Act. The court held that the purpose of the notice requirement in the APA was satisfied, and there was no Due Process violation if the party proceeded against "understood the issue" and "was accorded full opportunity" to justify its conduct.

In the absence of action by an agency promulgating rules or issuing interpretations, a court may find it necessary to determine what the agency would have done, had it in fact acted. The federal courts occasionally must do this with respect to cases which require the application of state law, but where the

state courts have yet to issue an authoritative ruling or interpretation on the point at issue. See, for example, *Stenberg v. Cinema N' Drafthouse Systems, Inc.*, 28 F.3d 23, 24 (5th Cir. 1994) (5th circuit "predicts" Texas Supreme Court's probable decision concerning pre-default waivers by guarantors). Such decisions are not considered binding upon the state courts where they later have occasion to actually rule on the point.

The judicial supremacy of the federal courts over agencies is limited to determinations of constitutionality and the actual resolution of disputes. *Marbury v. Madison*, 5 U.S. 1 (Cranch) 137 (1803), establishes the federal judiciary with the U.S. Supreme Court at its apex as the "ultimate interpreter of the Constitution." *Baker v. Carr*, 369 U.S. 186, 211 (1962). See Tribe, *American Constitutional Law* § 4-11, pp. 729-30 (3d ed. 2000).

Once the U.S. Supreme Court has determined the "clear meaning" of a statute, the doctrine of *stare decisis* applies and a later interpretation of that statute by an agency must be judged against that prior determination. *Maislin Industries, U.S., Inc. v. Primary Steel, Inc.*, 497 U.S. 116, 131 (1990). However, an agency's interpretation of statutes it is authorized to administer is entitled to great deference from the courts and this is true even when the agency issues an interpretation that represents "a sharp break" with the agency's own prior interpretations. " (*Chevron U. S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 863-64 (1984); *Smiley v. Citibank (South Dakota) (N.A.)*, 517 U.S. 735 (1996); *Rust v. Sullivan*, 500 U.S. 173, 186-87 (1991)). See Tribe, *American Constitutional Law* § 5-19, pp. 997-1002 (3d ed. 2000).

Courts have stated that, because the Packers and Stockyards Act lacks any statutory definition of the phrase "Unfair, unjustly discriminatory or deceptive practice" that its meaning must be determined by the facts of each case within the purposes of the Act. *Capitol Packing Company v. United*

*States*, 350 F.2d 67, 76 (10th Cir. 1965), *Hays Livestock Commission, Inc. v. Maly Livestock Commission Company, Inc.*, 498 F.2d 925, 930 (10th Cir. 1974), *Capitol Packing Company v. United States*, 350 F.2d 67, 76 (10th Cir. 1965). However, these cases have also noted the indisputable proposition that a court faced with a question of statutory interpretation is bound to give "great deference" to any interpretation of the statute made agency charged with administration of the statute. This is, of course, consistent with the basic concepts of administrative law noted earlier and comports with the judicial recognition that "the responsibility for efficient regulation of market agencies and packers lies with the Secretary of Agriculture," *Capitol Packing, supra*, at p. 76.

Therefore, It is my opinion that the USDA has the legal authority to promulgate specific rules or specific proposed guidelines under the Packers and Stockyards Act, and that the USDA is not precluded from doing so by administrative guidelines or federal court decisions (other than specific rulings of the United States Supreme Court) interpreting them in absence of specific proposed guidelines.



## GUIDELINES

- (1) The term "unreasonable preference or advantage" shall include but not be limited to any practice or device by a packer, or packer's agent or representative, including a single transaction, to procure livestock, directly or indirectly, from a producer on terms offered to that producer while at the same time withheld from smaller volume producers unless such livestock is purchased within two weeks of slaughter in a public market through a competitive bidding process. Price differences that reflect differences in costs of acquiring and handling the livestock shall not be considered an unreasonable preference or advantage. Price premiums based on established and recognized standards for product quality, time of delivery and production methods that enhance product value shall not be considered an unreasonable preference or advantage provided that those premiums can be reasonably applied on a wide range of farm sizes and are offered in a manner that does not discriminate against smaller volume producers; and
- (2) The term "differences in cost of acquiring and handling livestock" shall not include any cost savings that result from packers running their operations at full or nearer to full capacity.

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UNIVERSITY OF  
**WISCONSIN**  
M A D I S O N

June 27, 2000

Charles Hassebrook  
Center for Rural Affairs  
P.O. Box 408  
101 S. Tallman Street  
Walthill, Nebraska 68067

Dear Mr. Hassebrook:

In an earlier memorandum, I concluded that the United States Department of Agriculture possessed the legal authority to promulgate specific proposed guidelines (attached) defining undue price preference and discrimination under the 1921 Packers and Stockyard Act and that, as a legal matter, the provisions of such guidelines need not follow past interpretations (in the absence of guidelines) of any judicial bodies other than the United States Supreme Court.

I have now been asked to consider what basis USDA must have to support the promulgation of the proposed guidelines. As I understand it, the question is posed because the guidelines would deal with preventing possible future conduct instead of addressing conduct that is now ongoing.

This issue raises some key aspects of administrative law; I treat them necessarily in general and summary fashion below, given the need for a speedy response.

In general, an agency engaged in formal or informal rule writing<sup>1</sup> is required to incorporate in the first rules a "concise general statement of their basis and purpose". The requirement is for the purpose of a reviewing court's need "to see what major issues of policy

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<sup>1</sup>There are, of course, some differentiations between rules and guidelines although sometimes they both are treated as being "regulations" in a generic sense. Here, I treat the proposed guidelines as rules because meeting the requirements for that category will satisfy requirements for all other categories.

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were ventilated by the informal proceedings and why the agency reacted to them as it did.”

*Automotive Parts & Accessories Ass'n v. Boyd*, 407 F.2d 330, 338 (D.C. Cir. 1968). An agency must be able to respond to well-supported arguments critical of the proposed rule and failure to do so may form the basis for reversal of the agency's regulations. See, e.g., *Portland Cement Ass'n v. Ruckelshaus*, 486 F.2d 375 (D.C. Cir. 1973).

Most judicial decisions that set aside agency rules do so on the basis that the rule is “arbitrary and capricious” within the meaning of §706(2)(A) of the Administrative Procedure Act. In its opinion in *Motor Vehicle Manufacturers Association v. State Farm Mutual Automobile Insurance Company*, 463 U.S. 29 (1983), the U.S. Supreme Court stated that a rule would be “arbitrary and capricious” if:

The agency has relied on factors which Congress has not intended it to consider, entirely failed to consider an important aspect of the problem, offered an explanation for its decision that runs counter to the evidence before the agency, or is so implausible that it could not be ascribed to a difference in view or the product of agency expertise.

A summary of the standards for valid regulations issued by an agency, then, is that the agency action must be within its mandated authority from Congress, the agency must provide a basis and purpose for its action, and the agency's proposed action must not be “arbitrary and capricious” as that term is defined by the courts. (There is, of course, a huge number of cases, treating the term “arbitrary and capricious” in the context of specific actions but the language from the *Motor Vehicle Manufacturers* case, *supra*, seems to reflect the Supreme Court's current interpretation of the phrase.)

It must be emphasized that the analysis above does not apply to general statements of

policy by an agency. General statements of policy are exempt from APA rulewriting requirements. Thus, in *Pacific Gas & Electric Co. v. Federal Power Commission*, 506 F.2d 33 (D.C. Cir. 1974), a challenge to an order in which the Federal Power Commission announced a set of priorities for allocating national gas among customers in the event of a shortage was rejected by the court because the court's analysis of the order led it to conclude that notwithstanding some ambiguous language, the order was intended to have the effect of a general statement of policy. Thus, the order need not have followed APA requirements and the order served the purpose of placing affected parties on notice concerning the agency's policy preferences at the time it issued the order.<sup>2</sup>

The question of what constitutes a proper factual foundation for action by an agency necessarily is related to that agency's jurisdiction and authority over practices. It is commonplace, of course, for an agency to issue a regulation to deal with conduct that has occurred and which the agency believes violates some aspect of the laws or policies administered by that agency. Nonetheless, the question of whether an agency may issue a regulation that attacks prospective as opposed to existing conduct is not necessarily foreclosed.

For example, the Clayton Act authorizes action by the government (the Department of Justice or the Federal Trade Commission) against "incipient" violations of the Sherman Act – that is, practices that do not violate the letter of the Sherman Act, although they may violate the spirit of the Sherman antitrust statute. Moreover, Section 16 of the Clayton Act permits injunctive relief by private parties "against threatened loss or damage by a violation of the

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<sup>2</sup>There is also an exception for legislative rules following APA requirements when there is "good cause" for omitting the requirements due to an emergency or immediate harm if issuance of the rule is delayed. See, e.g., *Nader v. Sawmill*, 514 F.2d 1064 (TECA 1975).

antitrust laws." See *Hawaii v. Standard Oil Co.*, 405 U.S. 251 (1971). A private party, under this statute (read in conjunction with Section 4 of the Clayton Act by the courts) must demonstrate an actual injury. *Cargill, Inc. v. Monfort of Colorado, Inc.*, 479 U.S. 104 (1986) because a private party would not be entitled to compensation in the absence of actual interest. Governmental bodies, of course, act in the public interest and not for recovery of damages, when issuing rules.

A further expansion of the incipency doctrine occurred when the U.S. Supreme Court, in *Fashion Originators' Guild of America v. Federal Trade Commission*, 312 U.S. 457 (1941) ruled that the FTC Act could be used to attack practices that were "incipient" violations of the Clayton Act – that is, an incipency (in terms of violation of the spirit but not the letter of the Clayton Act) of an incipency (violation of the spirit but not the letter of the Sherman Act).

Although some may argue that the "incipency" cases apply only to actual conduct, it is this writer's opinion that these cases provide a strong rationale for proactive regulation by agencies that preclude conduct that, if implemented, would violate the law administered by the agency in question. This would particularly be true in situations where the practices attacked by the regulation either had been engaged in by those who would be subject to the regulation or their counterparts in the past or where similar conduct by others not subject to the jurisdiction of the agency in question had been attacked successfully by an agency with jurisdiction over those others.

Given the responsibility of the Secretary of Agriculture for the efficient regulation of markets under the Packers and Stockyards Act, the authority of the USDA to issue the proposed regulations (per my earlier memorandum), and the virtue of proactive as opposed to reactive

regulation of markets, the proposed guidelines need only be within the realm of authority of USDA and cover conduct that would violate the Packers and Stockyards Act, if that conduct were practiced. Evidence of past conduct of the nature covered by the proposed guideline being subject to regulatory action in any forum would strengthen the basis for the agency's issuance of the regulation.

Sincerely,

A handwritten signature in cursive script, appearing to read "Gerald J. Thain".

Gerald J. Thain  
Consumer Law Professor

September 19, 2000

Center for Rural Affairs  
Attn.: Chuck Hassebrook, Director  
Walthill, NE 68067

RE: Packer pricing--livestock.

Dear Chuck;

As discussed by telephone, it seems that large suppliers of livestock have the benefit of better market pricing opportunities than smaller entities. The packers have been fairly aggressive in getting large producers to enter into some type of contract, especially on swine, which has had the real effect of negating "live auction" prices as bid for livestock.

Examples of what I am pointing out are cited below, to the best of my knowledge and I am not insuring 100% accuracy.

Swine enterprises:

Matrix contracts which allow producer and packer to share in downside risk of price market and similarly in the upside risk of the market. What happens here is a "window" price is determined and as the market falls below this price minimum (i.e. \$42/cwt), then packer makes up half the price drop. If the price moves above the window (i.e.: \$45/cwt), then packer pays to producer half the increase above the window. These have typically had a "ledger account" at zero or no interest charged and totally unsecured. The actual contract is somewhat more complicated, but essentially as presented. In the \$8.00 market of 1998, the matrix producers showed better cashflow to with pricing still in the \$20/cwt. This obviously kept some of the larger producers out there as their cash losses were one third the cash losses of the non contracted producer. The ledger contract does represent a "contingent" liability, rather it can be collected or not either way remains to be seen.

A hybrid of this was used by a producer with a \$42/cwt minimum price, \$46/cwt maximum price with the ledger accruing on the bottom side, producer receiving the set minimum price and payback on the ledger starting only after the top end price was met, and this at a price share. Interest on the ledger contract was set at 0%. Again looking at the 1998 price decline, while contingent liability was accrued, cashflow went uninterrupted for the producer.

In Northwest Iowa and Southwest Minnesota, producers had a cost plus contract with the packer, guaranteeing a slight profit without price risk on the livestock or inputs. If one could operate (or expand) with this program, the 1998 prices had no effect on cashflow.

With the packers and stockyards reporting program in place or contemplated today, the packer has represented to one 30,000 head butcher producer that they were not willing to enter into a ledger/matrix contract, cost plus agreement or a set price for a production

period, however they were willing to adjust the market basis for contracting future production against the futures markets by \$2.00/cwt. This is about a \$5/head advantage to this producer. Interestingly, they were not willing to offer a matrix on 30,000 head, but a competitor packer has authorized a matrix contract to a 1,000,000 head package consolidator. The disadvantage here is pricing set off of cash markets and feed/genetics requirements built into the consolidators program.

With cattle, these programs are not as sophisticated for the general producer. There have been rumors and pointed fingers at some Packers for contracting for the purchase, feeding and delivery of fed cattle, all financed by the packer except for the hard facilities. Most recently, we have had a large group represented by a consultant which has a cash floor price bid for the next six months. This floor is subject to the top side rise of the market only, with producer benefiting here. The producer gives up \$1-2/cwt for this floor, but has virtually 100% of his capacity protected without worrying about put/call options, futures contracts, et. They know the minimum price for the animals and can figure breakevens and purchase prices accordingly. This is not offered to the general feedlot or small producer. This program is not written, but standard practice for the parties involved and has withstood several tests of the market.

The non contracted producer has seen a week where the packers is out of the market, taking formula contracted cattle or livestock with other contracts, driving the cash price down significantly. If the packer has the option of knowing exactly his major supplies, then the non contracted producer is relegated to a residual supplier, suffering greatly the feast and famine price swings. Unfortunately the famine side seems to outweigh the feast side, but this simply means the packer is doing a great job of protecting their kill.....at the cost of smaller producers.

Chuck, we are concerned with the future for the small producer, even those significantly larger than a mom & pop operation. Margins are down with significant risk put on these operations without the opportunity for significant price increases due to pre-marketed livestock in both swine and cattle sectors.

This is my personal insight and not to be construed as a representation of any other sort. If possible, do not site my name or my business.

Sincerely



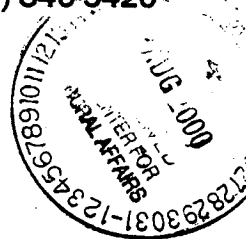


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## Contractual and Price Discrimination Narratives

Name: JERRY Heithoff

Email: glenalp@qpc.com.net

Address: Rt 1 Box 79

Phone: 402-843-2467

Dear Secretary Glickman—

As far back as 1994, I remember I was talking to the head man @ John Morrell for contracting hogs in advance. He told me the farthest I could go out would be 6 to 8 months. At that time I had heard of other producers locking in profits on their production in hogs, as far as 2 years in advance. I asked him about that, he told me I could do the 2 year contract, if I would guarantee him 200,000 hogs per year. At that time I was raising 2000/year. Today, I'm not raising hogs. If the USDA wants us to use risk management tools, then why aren't they allowing ALL producers that choice! BE the MAN of the Hour, not

Signed: Jerry Heithoff

Date: 8-20-00 (216)

the pin head of the Century"  
(Ted Roosevelt)

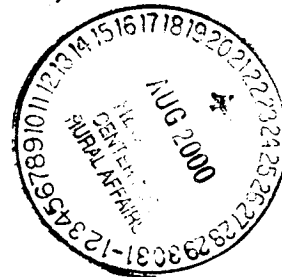


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## Contractual and Price Discrimination Narratives

Name: John Arens

Email: \_\_\_\_\_

Address: 55609 875 RD

Randolph Ne. 68771  
Phone: 402 586 2395

Dear Secretary Glickman—

I have been discriminated against by Harmel Foods because I market less than 10,000 hogs a year. They have two prices, one for less than 10,000 and one for more than 10,000. This is not a land of equal opportunity anymore!

Back in December of 1998 I had 150 hogs sold to Farmland two weeks before they were to be delivered. The day before they were to be delivered my Farmland representative called me and said I could only deliver 75. When I asked why he said "contract hogs came first." This is another discrimination act and certainly not a free open market system.

Signed: John Arens

Date: 8-20-00 (216)



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## Contractual and Price Discrimination Narratives

Name: Larry Dwecht Email: \_\_\_\_\_

Address: 300 Water St. Ogala, SD 57633

Phone: 219-665-2534

Dear Secretary Glickman—

When I was trying to make a decision as to try to stay in the hog raising or get out, I talked to Irvin Packer at Salomange, about how to get a contract and was told there were whole contracts and 1/2 contracts.

I don't remember the figures since it has been several months ago, however the guaranteed price was considerably higher on a contract.

I believe the figure was about 50,000 lbs of meat not hogs in the mouth of the contract. If you could produce this amount you knew ahead of time what you would be paid.

Signed: Larry Dwecht Date: 8/28/00 (216)



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## Contractual and Price Discrimination Narratives

Name: Jeff Schmitt

Email: \_\_\_\_\_

Address: 20626 Schmitt Ln Holy Cross, Ia 52053

Phone: 319-870-2285

Dear Secretary Glickman—

I am a Hog Producer who markets about \$400,000 in gross hog sales from a 500 sow herd! Friends of mine who are hog buyers for two different packers have reported to me bids on a base price difference of 1 to 2 Dollars a hundred weight advantage for the mega producers, Iowa Select, Murphy, etc! To my operation this results on an annual basis using the average advantage which would be \$1.50; approximately \$14,062! If this isn't price discrimination, I don't know what is.

Some day if consolidation keeps happening & a few companies, (my prediction is grain companies) will also own <sup>Control</sup> the livestock sector; this will be the end of ~~cheap~~ food for America; for, isn't this your goal??? Wake up?

Signed: Jeff C Schmitt

Date: 8-19-00 (216)

FLAG



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INCORPORATED

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## Memorandum

**To:** Center For Rural Affairs  
**From:** Lynn A. Hayes   
**Date:** February 22, 1999  
**Subject:** USDA's Authority for Mandatory Price Reporting

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The Secretary of Agriculture has the authority to implement mandatory reporting of slaughter hog prices and terms of procurement agreements under the Agricultural Marketing Act of 1946. He also has the authority to gather much more detailed information regarding hog prices and procurement methods to further his investigation and enforcement duties under the Packers and Stockyards Act (P&SA). Hog price and procurement information gathered under P&SA may be released if it is in the public interest.

### **A. Secretary's Authority to Issue Rules Mandating Price Reporting to the Agricultural Marketing Service**

The Secretary has the authority to require mandatory reporting of cash market prices and prices and terms of slaughter hog procurement by forward contracts, marketing agreements, and packer ownership/control arrangements to the Agriculture Marketing Service (AMS).

### **Legal Analysis**

The Agricultural Marketing Act of 1946 authorizes the Secretary of Agriculture to collect and report on livestock and meat prices. The congressional purpose for passing this Act is clearly expressed in the statute. Of primary concern to Congress was that USDA marketing programs, including the price reporting programs, be designed to improve the profitability of American farms and the orderly distribution of the commodities they produce and to reduce the price spread between the producer and the consumer. The express congressional purpose is:

[T]hat marketing methods and facilities may be improved, that distribution costs may be reduced and the price spread between the

producer and consumer may be narrowed, that dietary and nutritional standards may be improved, that new and wider markets for American agricultural products may be developed, both in the United States and in other countries, with a view to making it possible for the full production of American farms to be disposed of usefully, economically, profitably, and in an orderly manner.

7 U.S.C. § 1621 (emphasis added).

Pursuant to the Act:

The Secretary of Agriculture is directed and authorized . . . (g) to collect and disseminate marketing information, including adequate outlook information on a market area basis, for the purpose of anticipating and meeting consumer requirements, aiding in the maintenance of farm income and bringing about a balance between production and utilization of agricultural products.

7 U.S.C. § 1622(g) (emphasis added). The Secretary has the authority to promulgate rules he finds appropriate to implementing this statutory provision and which further congressional intent to improve profitability for livestock farmers, to ensure orderly disposal of their animals, reduce price spread between producer and consumer, and to bring about a balance between production and utilization of agricultural products. 7 U.S.C. § 1624 (b).

### **Evidentiary Basis**

AMS Market News livestock and meat price collection and reporting systems are voluntary. Those buyers and sellers contacted by USDA for price information are not required to report any information. They may choose not to report at all or to report selectively. The recent trend is that the number of persons contacted are declining to participate in this voluntary reporting system. In addition, the dramatic increase in the use of captive supply slaughter hog procurement contracts and arrangements, the prices and terms of which are not included in the AMS reports, is resulting in price reports that do not reflect the majority of the transactions. Failure to report on prices paid for captive supplies creates a serious question as to whether the AMS Market News reports accurately reflect the true value of slaughter hogs.

The current AMS Market News livestock and meat price reporting programs are failing to meet the congressionally stated purposes of the authorizing Act. They have not improved marketing and price information. Rather, they have failed to provide any useful pricing information on the large percentage of hogs acquired through captive supply procurement methods. The current voluntary reporting program does not assist livestock producers to dispose of their animals profitably because it does not ensure that adequate or even accurate information about livestock values is made available to them.

The Grain Inspection and Packers and Stockyards Administration recently released evidence which demonstrates that the current voluntary price reporting program does not

always accurately reflect true transaction prices. GIPSA's "Western Cornbelt Hog Procurement Investigation" report states that the results from a comparison of the reported prices and average base investigation prices for live and for grade and yield hogs showed "that in some cases, the average price in the investigation sample was higher than the AMS reported daily high."<sup>1</sup> The report concludes that "[w]hile the use of kill dates rather than purchase dates for comparison limits conclusions that can be drawn, the analysis shows that the reported prices did not reflect actual transaction prices paid."<sup>2</sup>

In addition, the GIPSA report indicates that the base price as well as the premiums paid increased with increasing seller size. Since the vast majority of the hogs sold by the larger-size sellers were under forward contracts or marketing agreements, the prices and terms of which are not incorporated into the AMS price reports, the higher base price and premiums are not likely to be accurately reflected in those reports.<sup>3</sup> The dramatic shift in procurement practices in the hog industry over the last several years underscores the need for additional public information on the price and terms of captive supply contracts and arrangements. While there appear to be no official reports on the current level of captive supplies in the hog sector, it is generally understood that the vast majority of all hogs slaughtered are now acquired under some type of captive supply arrangement, whether it be through forward contracts, marketing agreements, or packer ownership.

The ever increasing spread between producer and consumer prices also demonstrates that AMS programs are not accomplishing the congressional goal of reducing that spread. USDA's Economic Research Service reports:

Pork farm-to-retail price spreads set a number of record highs in a short period in 1997 and 1998. Before 1997, the largest farm-to-retail price spread occurred in November 1994 at 151 cents per pound. In March 1997 the spread hit 152.6 cents, a new high. Starting in September 1997 and running through February 1998, a new record was set every month except November.<sup>4</sup>

The trend toward increasing pork farm-to-retail price spreads continued as record low hog prices occurred in late 1998 and early 1999.

The Secretary has broad authority to issue regulations on livestock and meat reporting programs that will improve marketing methods, reduce the price spread between the producer and the consumer, and ensure profitable and orderly disposal of livestock by American farmers. Given the current structure of the hog industry, meeting these

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<sup>1</sup> Grain Inspection, Packers and Stockyards Administration (GIPSA) report, "Western Cornbelt Hog Procurement Investigation," p. 7.

<sup>2</sup> Id.

<sup>3</sup> Id. at 6.

<sup>4</sup> Livestock, Dairy and Poultry Report, "Forecasting Farm-to-Retail Pork Price Spreads" by William F. Hahn, (July 1998).

congressionally stated goals necessitates establishment of a mandatory reporting system that will include information on both cash-market prices and terms and prices for all captive supply procurement methods, including forward contracts, marketing agreements, and packer ownership of hogs.

**B. Secretary's Authority to Gather and Report Price and Procurement Method Information under the Packers and Stockyards Act**

As part of his investigation and enforcement powers, the Secretary has the authority to require by special order that packers, stockyard owners, market agencies, and dealers file regular reports regarding all livestock transactions. Special orders may mandate that these reports include all important information regarding (1) method of procurement of slaughter hogs, including negotiated sales, spot market purchases, forward contracts, marketing agreements, and packer ownership arrangements; (2) terms of payment, including whether purchases were made on live-weight or carcass-merit basis, under fixed base-price contracts, formula-priced contracts, and/or with premium and discount formulas; (3) number of captive livestock in inventory and number of captive livestock slaughtered during specified periods; (4) practices for offering or entering into forward contracts, marketing agreements, and other captive supply arrangements; and (5) any additional information the Secretary deems necessary to carry out the provisions of the P&SA.

Information gathered from the reports received in response to such special orders may be made public on a regular basis in a form which does not disclose any trade secrets or privileged or confidential information.

Under this statutory authority, the Secretary should immediately (1) issue a special order requiring all packers to report the above-described types of information on a regular and continuous basis; (2) develop a system for analyzing the reported information to determine whether any violations of Section 202 of the P&SA have or are likely to occur; and (3) develop a public reporting system that would provide immediate disclosure of appropriate portions of these reports.

**Legal Analysis**

Under the Packers and Stockyards Act, the Secretary of Agriculture is authorized to mandate, by general or special orders, that packers, stockyard owners, marketing agencies, and dealers file "annual or special, or both annual and special, reports or answers in writing to specific questions, furnishing the . . . [Secretary] such information as . . . [the Secretary] may require as to the organization, business, conduct, practices, management, and relations with other corporations, partnerships and individuals." 15 U.S.C. § 46, incorporated by reference in 7 U.S.C. § 222. This statutory authorization has been incorporated into the Packers and Stockyards Administration Regulations which state that "each packer, . . . stockyard owner, market agency, and dealer, upon proper request, shall give to the Secretary or his duly authorized representatives in writing or otherwise, and under oath or affirmation if requested by such representatives, any information concerning the business



of the packer, . . . stockyard owner, market agency, or dealer which may be required in order to carry out the provisions of the Act and regulations . . . ." 9 C.F.R. § 201.97.

The Act also authorizes the Secretary to release information obtained through special orders to the public when disclosure is in the public interest and the information as reported does not disclose any trade secrets or privileged or confidential information.

The [Secretary] shall have the power — (f) to make public from time to time such portions of the information obtained by it hereunder as are in the public interest; . . . *Provided*, that the [Secretary] shall not have any authority to make public any trade secret or any commercial or financial information which is obtained from any person and which is privileged or confidential . . . .

15 U.S.C. § 46, incorporated by reference in 7 U.S.C. § 222.

GIPSA does require packers, stockyard owners, market agencies, and dealers to file annual reports on prescribed forms. 9 C.F.R. § 201.97. The information made public from these reports has been of very limited use to producers because of the time it takes to compile and disseminate the information. As yet the agency has not made use of the authority to issue special orders to continually monitor and investigate the procurement and pricing practices of the packers in a timely and effective manner.

Issuance of special orders mandating regular reporting of procurement methods and pricing information that will be used to further investigation and enforcement of the P&SA and publishing appropriate portions of these is consistent with congressional intent in enacting the Packers and Stockyards Act. The legislative history of the Act makes clear that Congress intended the Secretary to use his extraordinarily broad regulatory powers aggressively to prevent conditions under which packers could gain control of the livestock market and to *compel* packers to do business in a lawful fashion, and thereby to induce healthy competition.<sup>5</sup>

It is appropriate under this congressional standard for the Secretary to issue special orders mandating regular timely reports on procurement practices and prices. Only through continuous and timely investigation and monitoring of procurement practices and prices

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<sup>5</sup> Repeatedly the P&SA bill was described as giving the Secretary the authority "to prevent packers . . . from engaging in an unfair, unjustly discriminatory, or deceptive practice or device." H.R. Rep. No. 77, 67th Cong. 1st Sess. 2 (1921); 61 Cong. Rec. 1799 (1921); 61 Cong. Rec. 1868 (1921). The House report on several of the debated bills states that the Act seeks "to prohibit the particular conditions under which monopoly is built up, and to prevent a monopoly in the first place and to induce healthy competition." Hearings on H. R. 14, H.R. 232, H. R. 5032, and H. R. 5692 Before the House Committee on Agriculture, 67th Cong. 1st Sess. Ser. D. 26, (1921).

can the Secretary be in a position to *prevent* violations of and *compel* compliance with Section 202 provisions of the P&SA so as to ensure healthy competition in the hog markets.

### **Evidentiary Basis**

Recent GIPSA studies provide evidence that supports the need for continuous and timely reporting of key information on packer procurement practices and pricing. The GIPSA "Western Cornbelt Hog Procurement Investigation" report made several findings that justify timely and continuous investigation of whether packer pricing and procurement practices in the hog market comply with Section 202 of the P&SA. As examples, the report found that during the studied time period: (1) "average base prices and premiums increased with increasing seller size . . . [and the study] shows that larger sellers are receiving higher premiums over the base price for hog characteristics, increasing the gap in price received over smaller sellers"; (2) "the analysis shows that reported prices did not reflect actual transaction prices paid"; and (3) "marketing agreement transactions were most utilized by the largest sellers."<sup>6</sup> These findings call into question whether smaller producers are being unjustly discriminated against and whether larger producers are receiving undue preferences in both the procurement methods available to them and prices paid in violation of Section 202 of the P&SA. Also called into question is whether packers are using deceptive price reporting practices when providing price information to AMS.

Based on these and other findings, the GIPSA report concludes that "the differences found in prices paid among various types of marketing arrangements indicate the need for continued monitoring and investigation regarding existing and emerging procurement and pricing arrangements to ensure open, competitive slaughter hog markets."<sup>7</sup> This report also expressed need for further investigation to address other areas of concern including "differences in hog characteristics and prices by pricing and procurement methods and seller size, and if price reports reflect transacted prices."<sup>8</sup>

GIPSA's report entitled "Concentration in the Red Meat Packing Industry," issued in February 1996, also points to the need for continuous and timely monitoring and investigation of packer pricing and procurement methods in the hog sector. The "Vertical Coordination in Hog Production" study contained in that report concluded, based on survey results, that during 1993 the extent of packer-producer contractual relationships or packer-owned/controlled production was too small to have major competitive impacts. However, it

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<sup>6</sup> Grain Inspection, Packers and Stockyards Administration (GIPSA) report, "Western Cornbelt Hog Procurement Investigation," pp. 6-8.

<sup>7</sup> Id. at 7.

<sup>8</sup> Id. at 8.

acknowledged that that industry expected significant increases in long-term contracts and integration between 1993 and 1998.<sup>9</sup>

This study also acknowledged that while there may be some potential benefits to some participants from a more tightly linked market, there is also "potentially more limited market access for hog producers, and increased short-term price volatility for smaller producers and/or producers heavily reliant on spot markets."<sup>10</sup> Such potential impacts justify close monitoring of industry procurement and pricing practices to ensure that any limitation of access or price volatility for small producers is not a result of discrimination, preferential treatment, or manipulation of prices in violation of the P&SA.

The vertical coordination study also found that "packers' contracts were almost exclusively with the largest hog producers."<sup>11</sup> This finding calls into question whether the largest producers are granted undue preferences over other producers by being given almost exclusive access to the marketing contracts that the authors assert provide many competitive advantages.

The report concludes that "the increasing use of an expanding variety of vertical coordination mechanisms suggests the need for further analysis of specific marketing and production arrangements to assess their impact on producers' and packers' operation and on the competitive structure of the industry."<sup>12</sup> This conclusion highlights the need for the continuous and timely gathering of information about slaughter hog procurement and pricing practices in today's rapidly integrating industry.

These GIPSA reports provide adequate justification for issuance of a special order mandating regular and continuous reporting by packers of key information on procurement practices and prices. GIPSA needs such information to continue its investigations into industry practices to determine whether packers are complying with Section 202 of the P&SA.

### **Publication of Price and Procurement Information Is in the Public Interest**

Timely public reporting of appropriate portions of the information received from packers, in a manner that protects trade secret and privileged information, will enhance review and monitoring of industry practices and will provide a mechanism to improve competition in the industry and, therefore, is in the public interest.

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<sup>9</sup> Grain Inspection, Packers and Stockyards Administration (GIPSA) report, "Concentration in the Red Meat Packing Industry," p. 43.

<sup>10</sup> Id.

<sup>11</sup> Id.

<sup>12</sup> Id. at 44.

The public as well as producers benefit when there is effective and efficient public reporting of market information. Wayne Purcell, director of the Research Institute on Livestock Pricing at Virginia Tech, reports that the "public good" is served by effective and efficient reporting of market information because it reduces discounts for uncertainty in the market and results in improvement in resource allocation.<sup>13</sup> He gives two examples of how lack of adequate information in the livestock sector can adversely effect consumers:

Most livestock producers are risk averse to some degree, which means exposure to risk brings with it a discounting for that risk. This can take the form of a reduction or leftward shift in the supply that producers offer to the marketplace . . . *any decrease in industry supply that can be traced to a lack of market-related information means consumers face a smaller supply and higher prices than might otherwise be possible.* Consumers would benefit if better (or more complete) market information prompted a larger supply.<sup>14</sup>

The discounting for risk and uncertainty also occur on the demand side, and this may be the area where market news is of special importance. To the extent slaughter livestock producers have difficulty estimating the value (price) of their livestock because of inadequate market information, they discount for the uncertainty by trying to buy feeder animals at lower prices. Over time, this can cause the demand for feeder livestock to shift to the left (and/or rotate so that it is steeper). The result is what economists call a "deadweight social loss" due to imperfections in the market, and one important source of market imperfection is less than socially optimal levels of market information.<sup>15</sup>

After reviewing the limited studies dealing with the public value of gathering and disseminating market information Purcell concludes:

There is, then, a *public good* component to market information when price discovery is made more effective and more efficient by public market reporting activities. Getting to the "true" prices more quickly and with less error smoothes the process of reacting to informational shocks in the marketplace. Exposure to the risk of volatile prices throughout the system is reduced. There is, consequently, less discounting for uncertainty and a more efficient allocating of resources, all of which means larger supplies and lower prices to consumers. Since prices of agricultural commodities tend to approach the cost of production over time, lower prices to consumers do not

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<sup>13</sup> Purcell, Wayne D., Price Discovery in Concentrated Livestock Markets: Issues, Answers, Future Directions, "The Role of Market Information in Price Discovery and Market Structure" Chapter 5, pp. 125-133, (February 1997), Research Institute on Livestock Pricing, Department of Agricultural and Applied Economics, Virginia Tech.

<sup>14</sup> Id. at p. 126.

<sup>15</sup> Id.

translate into lesser profits for producers. Over time, the producers' resources will earn a return commensurate with their marginal contribution, and the sector will be bigger and command a larger market share in the presence of a well-informed marketplace and effective price discovery processes.<sup>16</sup>

Purcell also asserts that effective and efficient public reporting of market information also serves the public interest by helping to preserve an agricultural production system of independent entrepreneurial producers. Citing several studies, he argues that if producers do not have access to adequate price information regarding the "underlying supply-demand forces that determine the 'true' underlying but unobservable equilibrium price" there is a threat of "the 'failure' of the open market price-based systems."<sup>17</sup> As the open market price-based system fails to provide adequate signals to coordinate information vertically across functions, the price-based market will be replaced by contractual arrangements and integrated structures controlled by firms. He concludes:

*If society values an atomistic structure in production agriculture made up of many independent producers, then there is reason to seek to improve the performance and effectiveness of the pricing mechanism by improving information available to buyers and sellers—especially sellers.<sup>18</sup>*

### **C. Recommendations for Price and Procurement Method Reporting**

To further the investigation and monitoring of the hog sector, GIPSA should issue a special order requiring packers to report the following types of information:

1. Quarterly provide GIPSA copies of each type of forward contract, marketing agreement, production contract, and joint venture agreement used to procure slaughter hogs in the previous quarter and any such contracts intended to be used in the upcoming quarter. In an accompanying report provide a break-down of the producers participating in each of the attached contracts and agreements by size of producer. In this report also respond to questions developed by GIPSA addressing how these contracts are offered to producers including a the size of operations offered each type of contract, the extent to which access to each contract is limited by the producer's ability to deliver large volumes of slaughter hogs, whether the each contract requires a producer to sell all hogs produced to the packer, whether the packer or the producer has control of the delivery date under contract, and whether each contract contains any confidentiality provision.
2. Weekly report the volume of slaughter hogs held for future delivery under captive supply arrangements including forward contracts, marketing agreements, packer

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<sup>16</sup> Id.

<sup>17</sup> Id.

<sup>18</sup> Id. at 130.

ownership (including hogs raised on production contracts) and joint venture agreements by plant and/or marketing region, projected delivery date in semi-monthly intervals, price range categories, and price term categories including fix-base price, formula price, and grade and yield premium formulas.

3. Daily number of hogs slaughtered by plant including the percent of total acquired through each of the following procurement methods negotiated or cash market purchase, forward contract, marketing agreement, joint venture, and packer ownership (including animals raised under production contracts).
4. Daily price paid for slaughter hogs acquired through each of the following procurement methods negotiated or cash market purchase, forward contract, marketing agreement, joint venture, and packer ownership. The price reported for each category should include:
  - a. Whether paid on live-weight, carcass-merit, value in the meat, or other method to be described in the report.
  - b. For all negotiated or cash market purchases, the base price and a description of the types and amount of any premiums or discounts (including, but not limited to grade and yield, volume, early delivery, and percent lean) used to calculate actual pay price.
  - c. For all slaughter hogs procured through contract, the base price for all fixed-base (base price could be equated with a specific dollar amount at the time the seller entered the agreement to sell) contracts; the formula used to determine the base price on all formula-priced contracts and the actual price determined by the formula; and a description of the types and amount of any premiums or discounts (including, but not limited to grade and yield, volume, early delivery, and percent lean) used to calculate the actual pay price.
  - d. For all slaughter hogs procured through packer ownership (including those raised under production contracts) and/or joint venture, the actual price paid including a description of any base price formula and amount, and a description and amount of any premiums or discounts (including, but not limited to grade and yield, volume, early delivery, and percent lean).
  - e. All above information should be reported based on lot size delivered and producer size within ranges established by GIPSA (range categories should be reasonable and establish at least one high-end category that separates out the top 25 producers).
5. At the beginning of each week, the number of hogs committed through contract or ownership for delivery that week by plant.
6. All of the above information for slaughter hogs or carcasses imported by country from which imported.

7. All of the above information for slaughter hogs or carcasses exported by country to which exported.
8. Weekly report prices and volume of pork products by categories established by GIPSA sold domestically and for export.